Recent Trends in Unemployment Duration

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The recession that began in early 2001 probably has ended, as national output grew moderately during the first three quarters of 2002. Unemployment, however, remains a problem. Between late 2000 and early 2002, the national unemployment rate increased by about 2 percentage points, from 3.9% to about 6%; this represents about 2.8 million additional individuals looking for work. Thus far in 2002, payroll employment has been flat to down nationwide, and the unemployment rate has stayed stubbornly close to 6%, raising the specter of a "jobless recovery" from the 2001 recession. Persistent labor market weakness implies that the amount of time spent unemployed (unemployment duration) is likely to increase, which in turn has important implications for household well-being.

In this *Economic Letter*, I discuss the concept of unemployment duration, the various measures available, and the evidence regarding the pattern of unemployment duration in the current cycle compared to past cycles. Reliable measures of the expected length of unemployment spells indicate that although duration increased more than expected in recent months, it has not been especially long during the recent economic downturn. Underlying this may be the improved labor market conditions of the 1990s expansion, which acted to offset a long-term trend toward rising duration of unemployment.

Unemployment duration

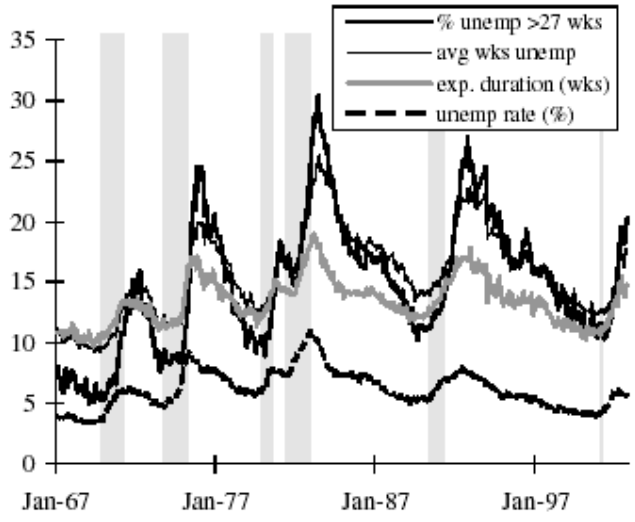
Unemployment duration refers to the amount of time that an individual remains unemployed. In the 1970s and 1980s, scholars and policymakers debated whether the typical unemployment spell in the U.S. is best described as "long" or "short." This distinction is critically important for assessing the economic efficiency and equity aspects of unemployment. The short view emphasized the dynamic nature of unemployment, focusing on job turnover and implying that the pool of unemployed typically is dominated by a large number of individuals who experience relatively short spells of unemployment (a month or two at most). This view generally is consistent with voluntary search activity by unemployed individuals and employer reliance on temporary layoffs for cyclical employment adjustments. In contrast, advocates of the long view argued that the pool of unemployed typically is dominated by individuals who experience relatively long spells of unemployment (three months or more) and are best described as "involuntarily" unemployed, often through permanent job loss. Thus, the two views pose the extremes of a well-functioning market for matching workers and employers in which the burden of unemployment is widely dispersed and a situation in which a relatively small number of workers bear the burden of a persistent shortage of appropriate jobs.

Of course, the truth about unemployment lies somewhere in between the extremes of short and long durations. No matter what duration structure characterizes unemployment under typical labor market conditions, however, the deterioration in labor market

conditions that occurs during a recession implies a cyclical increase in the incidence and share of long spells of unemployment. As recessions persist, rising unemployment rates are accompanied by rising unemployment durations. Although households can rely on savings to tide them over during short spells of unemployment, their ability to do so declines as unemployment spells lengthen. As such, rising unemployment duration during economic downturns can have adverse consequences for household spending and financial solvency and may act to stifle the recovery. Policy responses to recessionary unemployment therefore tend to focus on long spells--for example, in March 2002 Congress extended unemployment insurance benefits from 26 weeks to 39 weeks (up to 52 weeks in states with high unemployment rates). Such measures can reduce the hardship associated with long spells but may have the adverse side effect of lengthening unemployment by reducing the costs of job search.

Duration measures

Figure 1
Unemployment duration and rate



Note: The shaded areas and vertical line respectively represent recessions and a business cycle peak as defined by the National Bureau of Economic Research.

A variety of different measures of unemployment duration at the national level are available on a monthly basis, each based on data from the monthly household survey administered by the U.S. Census Bureau and Bureau of Labor Statistics (BLS). Figure 1 displays three of these measures for the period January 1967 to October 2002, plotted along with the unemployment rate as a standard indicator of the cyclical status of the labor market. Each of these measures is corrected for the changes in survey design implemented beginning in January 1994. These changes affected the measurement of unemployment duration and other labor force variables. To make the series used below consistent over time, I applied the adjustment factors described in Polivka and Miller (1998).

Perhaps the most commonly cited measure of unemployment duration is "average weeks unemployed," which is tabulated and released each month by the BLS. It measures the average duration of unemployment spells sampled while in progress, at the time of the survey. As seen in Figure 1, this series exhibits pronounced cyclical swings, rising from about 11-12 weeks at business cycle peaks to above 20 weeks shortly after the end of severe recessions.

Although it measures average duration for unemployed individuals at a point in time, the average duration series does not represent the completed duration of unemployment that a

newly unemployed individual can expect to face ("expected duration"). Because the average duration is calculated based on all in-progress spells, it contains both an upward and a downward bias with respect to the measurement of the expected duration for a newly unemployed individual. The upward bias occurs because longer spells, purely by virtue of their length, are more likely to be in the monthly unemployment sample than are shorter spells. The downward bias arises because the use of in-progress spells precludes measurement of completed spell durations. For example, an employee laid off owing to a plant closure might expect to be out of work for many weeks. However, in the person's initial phase of unemployment, the household survey will record an unemployment spell of just a few weeks. On average, the duration is measured about halfway through the spell.

Although the two biases can in principle cancel out, in recessions the upward bias tends to outweigh the downward bias, leading to an overstatement of expected duration for a newly unemployed individual. This dominance of the upward bias can be seen in part by examining the series representing the percentage unemployed for at least 27 weeks, also displayed in Figure 1. This measure of long-term unemployment exhibits especially wide cyclical swings, varying from around 10% during cyclical peaks to as high as 30% during severe recessions. The sharp increase in the measured incidence of long spells during recessions raises the level of the average duration measure well above the expected duration for newly unemployed individuals.

Estimating the expected duration for newly unemployed individuals is possible, however, through use of additional BLS unemployment duration figures. Valletta (1998) demonstrated a simple method based on a transformation of the percentage of all unemployed who have been unemployed fewer than five weeks in the survey month (new monthly entrants to unemployment). The cyclical properties of this constructed series are similar to those for estimates of expected duration that are based on more detailed and precise tabulations of individual duration experiences (see, e.g., Baker 1992). The simple estimate of expected duration, tabulated according to the technique in Valletta (1998), is displayed in Figure 1. It exhibits less pronounced cyclical swings than do the other duration measures, ranging from a low of about 10 weeks to a high of about 19 weeks. The upward bias in the average duration measure (as a measure of expected duration) can be seen in this figure: average and expected duration are close when the labor market is tight, but average duration substantially overestimates expected duration during periods of high unemployment.

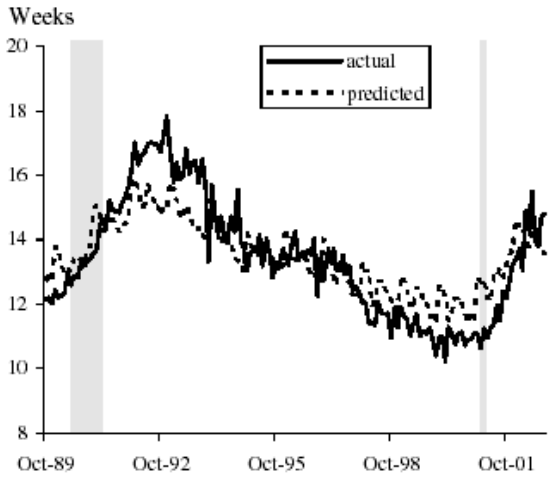
Is duration high or low in 2002?

Despite the persistence of the current slowdown, unemployment measures suggest that it is not as severe as the preceding three major recessions (1975-1976, 1982-1983, and 1991). The recent peak unemployment rate of 6.0% is well below the peaks reached in those earlier recessions. Consistent with this, each of the duration measures has remained below its peak in the three preceding recessions (Figure 1). For example, the expected duration of unemployment hovered around 15 weeks from June to October of this year, well below its peaks of about 18-19 weeks in the past two recessions. Given the recent

up-and-down movements in each of the three duration series, the direction of their movement in coming months is uncertain. However, the recent movement contrasts with a steady increase in preceding months, which suggests that a turning point may have been reached and unemployment duration will soon begin to decline. If so, the current slowdown in retrospect probably will be regarded as mild in terms of its effects on unemployment duration.

Another way to assess the severity of unemployment duration in the current slowdown is in purely relative terms. In particular, given the relatively low unemployment rate in the current recession compared to past recessions, it is useful to ask whether unemployment duration is long relative to the current unemployment rate and any long-term trends in unemployment duration. If the unemployment pool has a relatively large share of individuals with long spells, even with a low unemployment rate the uneven burden of unemployment can hamper economic recovery.

Figure 2
Expected duration of unemployment



Note: The shaded area and vertical line respectively represent a recession and business cycle peak as defined by the National Bureau of Economic Research.

Figure 2 addresses this issue by plotting the expected duration of unemployment based on observed data, as defined above, against its predicted value. To focus more clearly on the recent recessionary pattern, the figure displays values for the period October 1989 to October 2002. The prediction model, however, is based on data for the period January 1967 to May 1998 (the same sample as used in Valletta 1998). Thus, the predictions for the period June 1998 to October 2002 are "out of sample" forecasts based on the pre-existing relationships between the variables in the prediction model. This model incorporates only the unemployment rate and a trend over time as explanatory factors, so that the differences between the actual and forecast values represent a break from the pre-existing relationship between current expected duration and the unemployment rate or the long-run trend in expected duration. Measured independently of the unemployment rate, the long-run trend in duration is upwards; as reported by Valletta (1998), expected duration increased by about 17% (approximately 2 weeks) between 1976 and 1998.

The figure indicates that actual expected duration was below its predicted values during much of the late 1990s expansion and most of the recent slowdown to date. The excess of the predicted values over the actual duration indicates that unemployment duration was shorter than we would expect based on the level of unemployment achieved and long-term upward trend in duration. Thus, the economic expansion of the late 1990s may have produced favorable labor market conditions (such as effective job matching) that acted

against a pre-existing trend toward longer unemployment spells. On the other hand, since April of this year actual expected duration has been running a bit above its predicted values, suggesting recent deterioration in job prospects for unemployed workers. This may be only a temporary development, or it may signal that recovery in the labor market will be further delayed; only time will tell.

References

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